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Supreme Court, U.S.
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No. 01-1728

In the
Supreme Court of the United States

ELLETT BROTHERS, INC.,
Petitioner,

v.

UNITED STATES FIDELITY AND GUARANTY COMPANY,
FIDELITY AND GUARANTY INSURANCE UNDERWRITERS, INC.,
ST. PAUL MERCURY INSURANCE COMPANY,
Respondents.

ON PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

PETITIONER'S REPLY BRIEF

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REPLY FOR THE PETITIONER

Respondents contend that review by this Court is not warranted because both the district court and the majority opinion in the court of appeals correctly apply South Carolina law to determine that respondents are not obligated to defend the four lawsuits for which petitioner seeks coverage and indemnification. However, respondents' characterization of those opinions attributes to them a holding not actually reflected in either opinion, as neither the district court nor the majority made any meaningful attempt to discern – much less apply – South Carolina law.

To the extent that respondents claim that the result below is defensible insofar as it is consistent with South Carolina law as articulated in *Braswell v. Faircloth*, 387 S.E.2d 707 (S.C. Ct. App. 1989), respondents actually rest their defense not on the majority opinion, but instead on the *concurring* opinion of Judge Michael, who expressly *disagrees* with the majority's reliance on *Cincinnati Insurance Co. v. Milliken*, 857 F.2d 979 (4th Cir. 1988), and the default rule purportedly established therein. Moreover, respondents' attempt to explain away the discrepancies between Judge Michael's concurrence and the majority opinion as a "distinction without a difference" wholly misses the point of the Question Presented, as Judge Michael's concurrence – by seeking to discern and apply South Carolina law – does precisely what the majority does not.

Finally, the majority's failure to discern and apply South Carolina law sets a dangerous precedent for Fourth Circuit law, as the majority's reliance on the "default rule" allegedly established in *Milliken* has led to a disparity between state and federal courts with regard to South Carolina law.

I. Respondents' Brief in Opposition Rests on a Mischaracterization of the District Court Opinion and Dicta in the Majority Opinion.

Respondents attempt to defend the judgment below by asserting that both the district court and the majority opinions correctly apply South Carolina law and, based on this correct application, conclude that respondents are not obligated to defend the lawsuits for which petitioner seeks coverage and indemnification. Specifically, respondents – not once, but twice – describe the district court opinion as holding that "contracts of general liability insurance do not cover claims for *equitable relief aimed at preventing future injuries*." Brief in Opposition [hereinafter "BIO"] 1 (citing Pet. App. 20a-24a) (emphasis added); *see also id.* at 5 (explaining that "the district court awarded summary judgment in favor of St. Paul, finding that St. Paul was not obligated to defend [petitioner] . . . because, under South Carolina law, contracts of general liability insurance do not cover claims for *equitable relief aimed at preventing future injuries*" (citing Pet. App. 20a-24a) (emphasis added)). Similarly, respondents describe the majority opinion in the court of appeals as relying on *Milliken* to "enunciat[e]" a "rule . . . that amounts paid *to prevent future injuries* are not 'damages.'" *Id.* at 9 (emphasis added).

Unfortunately for respondents, the Brief in Opposition imputes to the district court and majority opinions a holding not actually reflected in either. Even a cursory review of both opinions reveals that the opinions rely solely on the "default rule" – allegedly established in *Milliken* – that the term "damages," as used in an insurance contract, includes only legal damages and excludes claims for equitable relief from coverage.

The district court's opinion, which relies completely on *Milliken*, holds only that respondents do "not have a duty to defend [petitioner] in the four pending lawsuits *because the relief sought in those cases is equitable in nature and, therefore, does not constitute damages*." Pet. App. 22a (emphasis added). Contrary to respondents' unequivocal description, the district court opinion thus makes absolutely no reference to the possibility that insurance contracts might in some circumstances cover claims for equitable relief, much less articulates a holding that might include some forms of equitable relief while excluding "amounts paid to prevent future injuries" (BIO 9).

The majority opinion explicitly holds only that "the term 'damages,' as used in [petitioner's] contract, does mean legal damages only, *and therefore does not extend to claims for equitable relief*." Pet. App. 8a (emphasis added). To be sure, having articulated this clear rule, the majority does note – in its discussion of "whether the four lawsuits against [petitioner] seek *legal damages*" (Pet. App. 8a (emphasis added)) – that none of the suits "seek compensation for past injuries" (Pet. App. 9a). However, in light of the majority's explicit legal/equitable distinction, the majority's passing statement in this context is more appropriately characterized as dicta, and certainly does not constitute a holding, in reliance on *Milliken*, that "amounts paid to prevent future injuries are not 'damages.'" *Contra* BIO 9-10. First, contrary to respondents' assertions regarding the majority's reliance on *Milliken* here, the majority could not have relied on *Milliken*, which made no such distinction between compensation for past and future injuries, to reach such a holding. *See* 857 F.2d at 981 (holding, without more, that "comprehensive general liability policies do not extend coverage to claims for equitable relief"). Indeed, the majority opinion cites *Milliken* in this Part only for the proposition that

restitution is an equitable remedy and therefore does not constitute "legal damages" for purposes of insurance coverage. *See* Pet. App. 9a. Second, and perhaps even more significantly, Judge Michael's concurring opinion – which, as discussed in greater detail below, holds that the lawsuits against petitioner did not constitute "damages" because the suits did not seek compensation for past injuries (Pet. App. 15a) – specifically declines to join not only Part I of the majority's holding, with regard to the legal/equitable distinction, but also Part II, which contains the very language cited by respondents as supporting the majority "rule" (Pet. App. 11a).

II. In Reality, Respondents Defend Judge Michael's Concurring Opinion, Which Expressly Disagrees With the District Court and the Majority's Reliance on *Milliken*.

As noted above, respondents' entire defense of the district court and majority opinions rests on the idea that those opinions correctly apply South Carolina law as articulated in *Braswell*, and based on this application hold that petitioner was not entitled to coverage or indemnification because the claims against it sought only equitable relief aimed at preventing future injuries.[1]

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[1] To the extent that respondents rely on other unreported South Carolina cases, such as *Helena Chemical Co. v. Allianz Underwriters Insurance Co.*, No. 96-CP-0343 (S.C. Ct. Common Pleas, Allendale County, Mar. 28, 2001) (BIO App. 1b-25b), and *Scheper v. U.S. Fidelity and Guaranty Co.*, No. 90-CP-07-879 (S.C. Ct. Common Pleas, Beaufort County, Oct. 29, 1991) (BIO App. 26b-49b), such reliance is similarly unavailing because the cases neither support the holding attributed by respondents to the majority nor – contrary to respondents' claim – provide any additional "guidance" regarding South Carolina courts'

However, an examination of the holding that respondents seek to defend reveals that respondents actually appear to be defending Judge Michael's *concurring* opinion. On the one hand, it is understandable that respondents might attempt to ally themselves with Judge Michael's concurring opinion, as Judge Michael (unlike the majority) undertakes a careful effort to discern South Carolina law and, based on his interpretation of the decision of the South Carolina Court of Appeals in *Braswell*, ultimately concurs in the result reached by the majority – that petitioner is not entitled to coverage. On the other hand, respondents' defense of Judge Michael's concurrence is nothing short of remarkable, as Judge Michael expressly *disagrees* with the majority on the very subject that is at the heart of the Question Presented: the *majority's* failure to discern and apply South Carolina law, relying instead on *Milliken* and the default rule purportedly established therein. *See* Pet. App. 12a.

Notwithstanding respondents' extensive discussion of *Braswell* in an effort to defend the decisions below, the majority opinion refers to *Braswell* only in passing (*see* Pet. App. 7a (erroneously citing *Braswell* as supporting *Milliken*'s holding that "[a]s a general rule comprehensive general liability policies do not extend coverage to claims for equitable relief" (alteration in original))). Instead, the majority relies almost exclusively on the Fourth Circuit's earlier decision in

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interpretation of the term "damages." Rather, both cases – which cite *Milliken* approvingly – merely hold that clean-up costs incurred to comply with government regulations are not "damages" covered under the relevant policies. *See* BIO App. 17b; *id.* 41b-42b. Indeed, neither opinion distinguishes between amounts paid to prevent future injuries and amounts paid to compensate for past injuries, as both cases involve attempts to recover costs incurred to clean up environmental damage *that had already occurred*. *Id.* 6b-10b; *id.* 27b-29b.

Milliken, in which the court of appeals – based on decisions interpreting Maryland and Missouri law – *predicted* that South Carolina courts would interpret the term "damages" so as to exclude claims for equitable relief. *See* 857 F.2d at 981 ("*We have no doubt that South Carolina law . . . would recognize* that a general comprehensive liability policy which obligated the insurer to pay 'all sums which the insured shall become legally obligated to pay as damages' would not cover claims for which the insured is equitably obligated to pay." (emphasis added)).

As Judge Michael's concurring opinion specifically acknowledges, however, the majority's blind reliance on the Fourth Circuit's thirteen-year-old holding in *Milliken*, without more, is inappropriate insofar as "South Carolina law . . . has not remained static since 1988" (Pet. App. 11a): "To the extent that South Carolina case law deviates from or contradicts our holding in *Milliken*, we must defer to the courts of South Carolina" (*id.* 12a). Judge Michael thus engages in a careful analysis of South Carolina law – an analysis, although in direct conflict with the majority opinion, with which respondents now seek to ally themselves – and, based on his analysis, concludes that "the ultimate holding in *Braswell*" – far from supporting the majority opinion, as both the majority and respondents contend – "appears to conflict with *Milliken*'s legal/equitable distinction." *Id.* 12a. Later in his opinion, Judge Michael describes the conflict in stronger terms, noting that "*Braswell* in effect rejects *Milliken*'s categorical rule excluding equitable relief from the term 'damages' because *Braswell* awarded coverage for environmental cleanup costs that the trial court had characterized as equitable relief." *Id.* 14a.

III. Judge Michael's Rejection of the Majority's Reliance on *Milliken* Is Not "a Distinction Without a Difference."

While expressly rejecting the majority's reliance on *Milliken* (and while noting its disagreement with the majority's failure to meaningfully discern and apply South Carolina law), Judge Michael nonetheless concludes that, although South Carolina law would award coverage for "equitable" relief in some circumstances, here petitioner is not entitled to coverage because none of the lawsuits against petitioner "sought [relief] to compensate for or repair past injuries" (Pet. App. 16a). In a footnote, respondents thus attempt to explain away the substantial discrepancy between the majority opinion, which relied on the legal/equitable distinction articulated in *Milliken*, and Judge Michael's concurrence, which specifically noted that the "default rule" on which the majority relies had been severely undermined, as "a distinction without a difference in this case because . . . there is no coverage for the Underlying Lawsuits under either view." BIO 10 n.3.

To the contrary, however, the distinction between the majority opinion and Judge Michael's concurring opinion is essential to the Question Presented, which ultimately seeks review of the majority's failure, contrary to *Erie Railroad Co. v. Tompkins*, 304 U.S. 64 (1938), to make any meaningful attempt to discern and apply South Carolina law. That Judge Michael – based on his analysis of South Carolina law – would have reached the same result as the majority opinion with regard to the availability of coverage for petitioner is of absolutely no relevance. Rather, if certiorari is granted, the court of appeals can consider on remand whether, when South Carolina law – as reflected in cases such as *Braswell* – is properly discerned and applied, the underlying relief warrants coverage.

Indeed, petitioner's case is on all-fours with *Devlin v. Scardelletti*, 265 F.3d 195 (4th Cir. 2001), *rev'd*, 122 S. Ct. 2005 (2002), in which Judge Michael concurred in part and concurred in the judgment. He disagreed with the majority's holding that an objecting class member who does not intervene lacks standing to appeal a settlement order, but he agreed with the result reached by the majority, explaining that in any event he would sustain the district court's decision to approve the settlement on the merits. *See* 265 F.3d at 213-16. In their Brief in Opposition to the Petition for Certiorari in that case, the respondents argued that certiorari was not warranted because – based on the majority opinion and Judge Michael's concurrence – "the ruling would have no practical effect on the final disposition of this controversy." No. 01-417, BIO 11 (filed Nov. 7, 2001). Notwithstanding the respondents' arguments, this Court granted certiorari, 122 S. Ct. 663 (2001), and subsequently reversed, 122 S. Ct. 2005 (2002), remanding to the Fourth Circuit for "further proceedings consistent with [the Court's] opinion." Thus, the mere fact that Judge Michael agrees with the result in this case, in light of his express disagreement with the majority's blind reliance on *Milliken*, hardly renders the discrepancies between his concurring opinion and the majority a "distinction without a difference" and should not preclude this Court from granting certiorari.

IV. Allowing the Majority's Opinion to Stand Would Set a Dangerous Precedent for Fourth Circuit Law.

Certiorari is further warranted because the majority opinion, if allowed to stand, would set a dangerous precedent for Fourth Circuit law by allowing panels in that circuit to ignore state law – even when clearly articulated by state courts – in favor of so-called default rules established by federal

courts. Such a result would not only be contrary to this Court's holding in *Erie*, but it would also perpetuate precisely the circumstances that *Erie* sought to avoid: forum-shopping based on the disparity between South Carolina law as interpreted by federal courts – here, upholding the legal/equitable distinction in coverage disputes – on the one hand, and South Carolina law as set forth by South Carolina courts, which have rejected such a distinction, on the other hand.

Moreover, if the majority opinion is allowed to stand, this disparity between South Carolina law as interpreted by federal and state courts is likely to continue for some time, as federal courts will erroneously rely on it as an authoritative expression of South Carolina law rather than – as required by *Erie* – seeking to discern and apply state law on a case-by-case basis. *See* Dolores K. Sloviter, *A Federal Judge Views Diversity Jurisdiction Through the Lens of Federalism*, 78 VA. L. REV. 1671, 1681-82 (1992) ("[S]ome evidence suggests that federal courts have shown a preference for citing federal decisions on state law instead of state decisions at rates approaching pre-*Erie* levels."). Indeed, to find an example of a federal court's reliance on federal decisions on state law, one need look no further than the district court opinion in petitioner's case, which makes no attempt to discern South Carolina law but instead relies solely on the Fourth Circuit's decision in *Milliken* to support its conclusion that "under [the Fourth Circuit's] interpretation of South Carolina law, *which the Court is bound to follow*, [respondents] do[] not have a duty to defend plaintiff in the four pending lawsuits because the relief sought . . . is equitable in nature and, therefore, does not constitute damages." Pet. App. 22a (emphasis in original). Further, not only does the district court opinion fail to mention state court cases such as *Braswell*, but it actually indicates – contrary even to respondents' concession that

Braswell is controlling law in the absence of a ruling from the Supreme Court of South Carolina, see BIO 8 n.2 – that it would not in fact regard a case such as *Braswell* as controlling, explaining that "[u]ntil such time (if ever) that the Fourth Circuit overrules [*Milliken*] (or there is some positive sign from the Supreme Court of South Carolina that [*Milliken*] incorrectly states the law), the Court will continue to apply the case as it has done here." Pet. App. 23a.

CONCLUSION

For the foregoing reasons, as well as those stated in the Petition for a Writ of Certiorari, certiorari should be granted.

Respectfully submitted,

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